No. 96-1660

In the Supreme Court of the United States

OCTOBER TERM, 1996

DONNA E. SHALALA, SECRETARY OF HEALTH AND HUMAN SERVICES, PETITIONER

v.

STATE UNIVERSITY, d/b/a OHIO STATE HOSPITALS

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

REPLY BRIEF FOR THE PETITIONER

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In the Supreme Court of the United States

OCTOBER TERM, 1993

No. 93-696

DONNA E. SHALALA, SECRETARY OF HEALTH AND HUMAN SERVICES, PETITIONER

v.

OHIO STATE UNIVERSITY, d/b/a OHIO STATE HOSPITALS

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

REPLY BRIEF FOR THE PETITIONER

Respondent does not dispute that the court of appeals' interpretation of the anti-redistribution provision at issue in this case conflicts with that of the Third Circuit that is before this Court in *Thomas Jefferson University Hospital* v. *Shalala*, petition for certiorari pending, No. 93-120 (filed July 20, 1993). See 93-120 Gov't Br. 9-10; 93-696 Pet. 7-8. Nor does respondent dispute that the question presented concerning the reimbursement of graduate medical education (GME) expenses is one of recurring

importance under the Medicare Program that warrants review by this Court. See 93-120 Gov't Br. 10-12. Respondent instead argues that the petition in this case should be denied because the legal issue on which the circuits are divided need not have been reached on the facts of this case. Respondent is wrong regarding the factual posture of the case. And, in any event, the Sixth Circuit did decide the legal issue, and our certiorari petition seeking review of its ruling therefore should be held pending the disposition of the petition and the decision in *Thomas Jefferson* on the same question.

1. In arguing that the Court should not hold this case pending the disposition of *Thomas Jefferson*, respondent presents a distorted picture of the administrative and judicial decisions below. Contrary to respondent's suggestion (Br. in Opp. 5), the district court's decision cannot fairly be read as making a definitive ruling on the factual issue of whether the medical school affiliated with the provider, respondent Ohio State University Hospitals, had ever previously absorbed a portion of the GME-related overhead costs for which the provider was seeking Medicare reimbursement. Moreover, the court of appeals was silent concerning the factual issue of whether the medical school had historically absorbed any of the GME-related overhead costs incurred at the medical school and claimed by the provider for the first time in 1985.

Neither court below had any occasion to identify the previous sources of financial support for the provider's GME programs, because both courts interpreted the final clause of the anti-redistribution

regulation, 42 C.F.R. 413.85(c),[1] as permitting Medicare reimbursement for the costs of all GME-related activities that contribute to the quality of patient care in the year for which reimbursement is sought. See Pet. App. 19a (stating district court's conclusion that the regulation bars reimbursement only of "purely educational costs unrelated to patient care, such as the cost of undergraduate medical education programs or nonclinical graduate medical education programs."); *id.* at 5a (similar conclusion by court of appeals). On this reading of the anti-redistribution regulation, the provider hospital's entitlement to reimbursement for all direct and indirect GME-related costs, including those incurred by an affiliated medical school, would not depend on which entity had previously absorbed or paid those costs, but only on the type of costs that were claimed. Thus, it would not matter whether the costs incurred in connection with the hospital's GME program had previously been paid by the medical school, the provider hospital, or by some other outside source of funding.

In contrast, the Administrator of the Health Care Financing Administration (acting for the Secretary of Health and Human Services) ruled that reimbursement for the GME-related costs claimed by the provider would result in a redistribution of costs from the medical school to the provider, because the provider had failed to show that it had previously absorbed all the costs of GME-related services that

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[1] The pertinent clause of the anti-redistribution regulation states that "it is not intended that [the Medicare] program should participate in increased costs resulting from redistribution of costs from educational institutions or units to patient care institutions or units." 42 C.F.R. 413.85(c).

were provided by the medical school. C.A. App. 103.[2] Accordingly, the Administrator concluded that to grant Medicare reimbursement to the provider for "[t]he overhead cost of the medical school" would result in "a redistribution of costs in violation of 42 C.F.R. 413.85." *Ibid.*[3]

2. To be sure, the district court appeared to disparage the Administrator's conclusion that, because the provider had failed to prove that it had previously paid all the GME overhead costs it was now claiming, the medical school must have absorbed these costs in the past. See Pet. App. 14a-15a, 19a-20a. But neither court below overturned the Secretary's factual determination on that issue. Even if the Administrator's conclusion on that factual issue was erroneous, however, this case should still be held pending this

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[2] The Administrator pointed out that "although the Provider has alleged that it has always paid these costs, it also stated that these costs have been absorbed by the provider *and* the college [of medicine]" in previous years. C.A. App. 99. The Administrator further stated that "[t]he record does not support the allegation that the Provider incurred these costs in prior years," pointing out that "[t]his information is within the purview of the provider." See also *id.* at 103 (formal finding of fact that the provider "did not demonstrate that the overhead costs of the medical school were paid by the provider in prior years").

[3] The Administrator also denied reimbursement on the alternative ground that, even apart from the prohibition on redistribution, the claimed "overhead cost[s] of the medical school are not allowable costs for Medicare purposes." C.A. App. 103. That ruling was reversed by the district court and was not challenged by the government on appeal. It is therefore not at issue in this Court.

Court's disposition of the petition in *Thomas Jefferson*.

The question presented in *Thomas Jefferson* is whether the Secretary may apply 42 C.F.R. 413.85(c) to bar a hospital from obtaining Medicare reimbursement of otherwise reimbursable GME program expenses that were found to have been absorbed in previous years by its affiliated medical school. See *Thomas Jefferson* Pet. App. 22a ("It is uncontroverted that the excess costs claimed by the Hospital in fiscal year 1985 previously were borne by the Medical School."); see also *id.* at 19a. The Third Circuit in that case relied on two separate grounds in holding that the provider was not entitled to reimbursement for previously unclaimed GME-related costs. First, it held that the final clause of the anti-redistribution regulation, which forbids the shifting of costs from an educational institution to a patient care institution, barred reimbursement of costs that had previously been paid by petitioner's affiliated medical school. *Thomas Jefferson* Pet. App. 20a-22a. The Third Circuit's holding on that issue is directly contrary to the Sixth Circuit's decision in the instant case. See Pet. App. 4a-6a. The Third Circuit further held in *Thomas Jefferson* that to reimburse the provider for previously unclaimed GME-related costs would violate the broader "community support" principle in the regulation, which the Secretary had interpreted as barring Medicare reimbursement to a provider for educational costs previously paid by the provider out of funds received from sources in the community at large. See 42 C.F.R. 413.85(c). Specifically, the Third Circuit agreed with the Secretary that, because the provider had not previously received Medicare

reimbursement for those services, it was appropriate to infer that the costs of those services must have been paid using funds provided by other sources in the community. See *Thomas Jefferson* Pet. App. 17a-18a. The court stated that the "universe of community support" could include not only the provider's affiliated medical school (which had absorbed the cost of the services in *Thomas Jefferson*, see *id.* at 19a, 22a), but also other funds received by the provider or its affiliates from outside sources that were then used to support educational activities. See *id.* at 18a ("community support" can consist of "tuition and fees, Federal appropriations, Federal grants and contracts, private gifts, grants and contracts, endowment income, investment income and other income").

Thus, even if the court in *Thomas Jefferson* had rejected the Secretary's interpretation of the anti-redistribution clause of the regulation, the provider hospital could still have been barred from receiving Medicare reimbursement for those costs because the costs would have been paid by the provider (or by the medical school) out of funds received from the community. And even if the Third Circuit had found in *Thomas Jefferson* that the newly claimed GME-related costs had previously been absorbed by the provider, rather than by the medical school, the community support principle might still have barred Medicare reimbursement to the provider for those costs, since a provider presumably must rely on such other sources of funds to cover expenses that are not reimbursed by Medicare.

In light of the foregoing analysis, if this Court grants the petition for a writ of certiorari in *Thomas*

Jefferson, it will almost certainly be appropriate to reverse and remand the court of appeals' decision in this case for further consideration regardless of how *Thomas Jefferson* is resolved. If the judgment of the Third Circuit in *Thomas Jefferson* is affirmed on the redistribution issue, the decision in this case will have to be remanded for a definitive determination of whether some portion of the costs claimed by the provider were in fact previously absorbed by the provider's affiliated medical school. To the extent the medical school had paid those costs, the provider would not be entitled to reimbursement, because the claimed amounts would represent "increased costs resulting from redistribution of costs from educational institutions or units to patient care institutions or units." 42 C.F.R. 413.85(c).

If, in contrast, this Court disagrees with the Third Circuit's resolution of the redistribution issue and concludes that reimbursement of the GME-related costs in that case would not represent a forbidden shift of costs from an educational unit to a patient care unit, the Court presumably would then consider the court of appeals' alternative "community support" rationale for holding that the provider was not entitled to reimbursement for GME-related overhead costs in that case. If this Court then upholds the Third Circuit's determination that reimbursement should be denied on the alternative ground that, under the regulation, the claimed costs had previously been paid by the "community," see *Thomas Jefferson* Pet. App. 17a-20a, it would be appropriate to vacate the decision in the instant case and remand for the Sixth Circuit to determine whether the community support principle remains as an independent obstacle to

reimbursement of the costs claimed by respondent.[4] In sum, since any decision in *Thomas Jefferson* will almost certainly have some bearing on the proper resolution of the instant case, the petition in this case should be held pending this Court's disposition of the petition in *Thomas Jefferson.*

For the foregoing reasons and those previously stated in the petition, the petition for a writ of certiorari should be held and disposed of in light of the Court's disposition of *Thomas Jefferson University, d/b/a Thomas Jefferson University Hospital* v. *Shalala*, petition for certiorari pending, No. 93-120.

Respectfully submitted.

DREW S. DAYS, III
Solicitor General

DECEMBER 1993

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[4] Respondent contends (Br. in Opp. 7) that there is no "square conflict" between the Sixth Circuit's decision in this case and the Third Circuit's decision in *Thomas Jefferson* because the court of appeals here did not separately discuss the community support principle, but based its holding solely on its interpretation of the anti-redistribution clause of the regulation. Respondent's reasoning is flawed. Not only is there a square conflict between the two decisions on the proper interpretation of the language in the regulation forbidding the shifting of costs from an educational to a patient care institution, but, as already explained, this Court's resolution of the community support issue would also shed light on the proper meaning of the regulation in its entirety and the proper application of the regulation in this case.